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Rescaling and Reforming the State under NAFTA: Implications for Subnational Authority

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Introduction

There has been a wide and active debate on the rescaling of geographic political and economic power under globalization. Some argue the role of the nation state is shrinking or being 'hollowed out' as national power shifts upward to international agreements, such as the World Trade Organization (WTO) and North American Free Trade Agreement (NAFTA), and downward to state and local governments through the process of decentralization (Brenner, 1999). This creates a space for the potential resurgence of the city as it deals directly with the external world (Swyngedouw, 1997; Brenner, 2000; MacLeod, 2001). Others see the neoliberal marketization process as one involving a reforming of the nation state — enhancing its penetration into market administration but in ways different from the protectionism of the past (Blanchard *et al*., 1998; Schamis, 2002).

This article explores the nature of this rescaling process at the national, regional and local levels using examples from the North American Free Trade Agreement (NAFTA). We argue that governmental authority is being eroded at the subnational level, while the national level is being reformed to accommodate global economic interests. A new governance nexus is forming — composed of international agreements, nation states and private corporations — which enhances the primacy of national over subnational governance scales. The goal of trade agreements and treaties is to limit the interference of governments in the free flow of goods and capital. Each limit on government action is by its nature a concession of sovereignty. The party that negotiates those concessions is therefore in a powerful position to change the intergovernmental balance of power and the relationship between commercial entities and the government. We present case studies at the national, state and local levels in the United States and Mexico to show how NAFTA is eroding subnational government authority in legislative and judicial arenas. We choose NAFTA as our example because other free trade agreements including the Free Trade Area of the Americas (FTAA) and a growing number of bilateral agreements replicate the new governance features first articulated in Chapter 11 of NAFTA. Urban and governance theorists need to give attention to this rescaling of governance and the unique role played by the nation state in orchestrating international agreements that delimit the scope for subnational action:

> we need to rethink our theoretical approach to the state so as to unravel its often clandestine role as a key site, function and orchestrator of globalization: a role that indeed lends shape to globalization's own political economic geographies (MacLeod, 2001: 823).

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Reforming the state

Neoliberalism promotes the use of market approaches to address public service delivery and the use of decentralization to promote accountability and responsiveness in government. Both decentralization and privatization reflect a shift away from government control and toward more competitive, market-style solutions (Bennett, 1990). Such approaches, according to public choice theorists, promote greater efficiency, accountability and responsiveness through the introduction of competition (Savas, 2000).

Under neoliberal globalization, the nation state is seen for its productive force — over its social or redistributive role (Brenner, 2000) — and cities are increasingly left to cope on their own (Jessop, 1997; Katz, 2001). In some cases, scholars point to a new importance for subnational forms of governance and a resurgence of the city (Swyngedouw, 1997; Le Galès, 1998; Brenner, 2000). Although the global and local are intertwined, we argue the global and national scales are privileged as these are the arenas where rules disciplining governments are set. The nation state retains a powerful mediating role in crafting disciplines that regulate market processes and capital flows (Jessop, 1997; Cerny, 1999). Urban scholars have expressed concern over the implications for uneven development and social cohesion (Amin and Graham, 1997; Fainstein, 2001), and have called for analysis of this process of rescaling as central to urban scholarship (Brenner, 2000). A core question, posed by Brenner and Theodore (2002: 342), is: 'Does the local really serve as a site of empowerment in the new global age, or do contemporary discourses on globalization/localization in fact conceal a harsher reality of institutional deregulation, regulatory downgrading, and intensifying zero-sum interspatial competition?'.

The provision of public goods is a core function of cities. Identifying collective needs and overcoming free riders and externality problems are primary roles of subnational governments. The new public management argues that markets can provide many public goods either through government contracting or through the structuring of Coasian bargaining relationships (Tiebout, 1956; Kettl, 1993; Webster, 1998; Savas, 2000). However, empirical analysis points to the importance of state and local governments in setting the terms of market engagement, i.e. playing a market structuring role (Sclar, 2000; Warner and Hefetz, 2001; Hefetz and Warner, 2004). When a government contracts for public goods it is not merely one customer among many, the contracting process is more typical of a quasi-market where government is the primary or sole consumer (Lowery, 1998).

Interestingly, enthusiasm for market solutions among neoliberal advocates has resulted in insufficient attention being given to government's market structuring role. The use of market approaches does not imply a retreat of the state, as many scholars have argued (Bennett, 1990; Osborne and Gaebler, 1992; Savas, 2000), but, rather, a new role. Rhodes (1996) and Salamon (2002) describe the complexities of government management of interdependent networks of private, public and non-profit actors. The need for collaboration and trust to maintain these networks over time undermines competition. Empirical analysis of privatization points out that competition frequently erodes under government contracting (many government services being natural monopolies) (Kodrzycki, 1994; Sclar, 2000). Network governance fundamentally alters the social contract between citizen and government and raises serious questions about accountability (Guttman, 2000; Salamon, 2002). Consumer choice differs in fundamental ways from citizen choice (Starr, 1988; Lowery, 1998), and market approaches to governance restrict rather than enhance public participation and community building (Frug, 1999; Denhardt and Denhardt, 2003). Ironically, the use of third parties requires an *expansion* of government oversight into the administration of markets to ensure that public values (accountability, equity, collective welfare) are met (Blanchard *et al*., 1998). Schamis (2002) uses Latin American examples to show how privatization is best understood *not* as a retreat of the state but rather as a reforming to manage market networks and ensure global competitiveness. To fully understand this

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reforming process, we need to look at changes in the authority of actors at different scales in the governance system.

In this article we illustrate this reforming process by showing how governmental authority is being centralized upward to the global and national levels even while privatization and decentralization open new opportunities for subnational and local governments. We use the North American Free Trade Agreement (NAFTA) and cases at the subnational and local level to illustrate key features of this governance rescaling and reformation process.

We will show that the regulatory structures created by the new free trade agreements falsely assume a competitive market in the provision of public goods and undermine subnational governments' ability to play a market structuring role. This creates a fundamental contradiction — making privatization a less viable option for urban service delivery while at the same time requiring further privatization of public goods provision. Subnational governments, though encouraged to directly engage global corporations in promoting economic development and public service delivery, do not have a formal role in crafting the rules that govern these relationships. The free trade agreements are negotiated by the executive branch of national governments and set new governance standards and protocols. National legislative and judicial oversight is limited and subnational governance mechanisms are rendered irrelevant. Yet it is at the subnational level where the contradictions between global competitiveness and public welfare will appear.

The North American Free Trade Agreement: new governance features

During the last decade the United States has pursued several multinational free trade agreements. The North American Free Trade Agreement, which came into force between Canada, Mexico and the United States in 1994, promulgated new governance features which have served as the governance template for subsequent free trade agreements (US–Chile FTA and FTAA). These features include expansion of the definition of barriers to trade to include basic subnational governance functions, expanded protections of private property and foreign investor rights, and the substitution of a private adjudication process for the public courts.

These changes represent a shift in the balance of power between subnational governments and the nation-state in the US context (Gordon, 2001), and introduce entirely new concepts in some Latin American countries (Esty, 1994). Unlike traditional treaties that focus on reducing tariffs or customs red tape at the border, this new generation of trade agreements introduces disciplines to eliminate government interference with profit and investment (Gordon, 2001). Many traditional local government regulations and guidelines are being reinterpreted as 'non-tariff barriers to trade' (Mann and van Moltke, 1999). Rather than respecting cultural and historical differences across space, the trade negotiators are attempting to homogenize legal standards and the criteria used by government for purchasing and contracting. This is a significant shift that allows the national and supranational scales to limit the flexibility of government at the municipal, state and local levels.

We present three cases that illustrate the nature of this rescaling at the national, regional (state) and local levels. These cases, drawn from recent and current NAFTA arbitrations, illustrate how these new governance features are being interpreted in practice. Data for our analysis come from the NAFTA text itself, and source material from published claims or final decisions. Unlike much jurisprudence, NAFTA panels are not bound to previous precedent, nor are they open to the public. Thus, there is no public record of the actual deliberations; the most that is released is the pleadings and final decision.

We have focused our analysis on NAFTA because, as the earliest free trade agreement and the one that first promulgated these new governance features, there has

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been the most time for cases to occur and, with them, an understanding of how these governance features will be interpreted in practice. These features are replicated in FTAA and many bilateral agreements, so our analysis of NAFTA is suggestive of challenges for the future. Each of these trade agreements is intended to promote market penetration in traditional public services and limit government control over market processes.[1] Our analysis shows that in this rescaling process, subnational governments still act with traditional powers, but can be trumped by the new governance provisions to which they are not party. We argue this creates a democratic deficit both at the global and national levels where these agreements are negotiated, and at the subnational (state and local levels) where they are implemented.

Case study 1: national-rescaling power — the NAFTA design process

United States, Canadian and Mexican representatives negotiated the terms of NAFTA for over five years and the FTAA has been in negotiation since 1995. The formal goals of the NAFTA agreement were to enhance trade among party nations by reducing tariff barriers, harmonization of laws so companies can expect similar regulations in each country and protection for private property from nationalization, and to avoid court systems in countries known for corruption. We show in the case below how the US approach to negotiations undermines shared power in a federalist system by privileging national interests in global competitiveness and appealing to international, commercial standards and processes that give priority to economic concerns over democratic representative ones. It is beyond the scope of this article to compare the constitutional provisions of the US, Mexico and Canada regarding division of power between federal and subnational government units. We rely primarily on US constitutional comparisons to illustrate how NAFTA represents a significant centralization in Federal executive power and erosion of legislative and judicial authority at the subnational level.

Treaties and trade agreements take on the authority of federal law and therefore subnational laws cannot be in conflict (US Constitution: Supremacy Clause, Article VI). This gives the agreements the power to trump subnational domestic policies. The US, Mexico and Canada are all federal systems with power shared between states or provinces and the national government, and power divided between the legislative, executive and judicial branches of government. NAFTA represents a shift in power to the executive branch of government by circumventing the courts and subnational legislation. These features advance the economic priorities of the nation, over concerns with legitimacy and democratic representation.

Negotiation process

The NAFTA has been credited with having an unprecedented level of public involvement, in part due to web postings of the draft texts and invitations for public written comments. At its core, however, foreign policy is the exclusive domain of the federal government (Lowi and Ginsberg, 2000). Worldwide, agreements are made in nation-to-nation negotiation, but the resulting obligations bind the subnational as well

1 The World Trade Organization, established in 1995 (144 countries), set new binding standards for governance of free trade agreements — subjecting non compliant nations to significant fines or sanctions. The General Agreement on Trade in Services (GATS) requires governments to select public services (like education, health, water, telecommunication, transportation, finance, energy and professional services) for commercial bidding and restricts mechanisms that give domestic companies or government agencies a competitive advantage. The Free Trade Area of the Americas (34 countries) is the next multilateral agreement to be decided, and it will extend these requirements to all public services except those specifically excluded (such as police).

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as national governments. Under the authority of the executive branch, the United States Trade Representative (USTR) represents the United States in the international Trade Negotiations Committee (TNC) (Kuehl, 2001a). Thirty industry-specific panels advise the USTR and one committee, the Intergovernmental Policy Advisory Committee (IGPAC), represents local government. While participation is broad, it is not public. All advisory meetings are confidential and limited to members only. Many of the industry panels have played a direct role in crafting the wording of the agreements, but the governance provisions have not been debated publicly — not even by the US Congress. Members of the IGPAC have expressed frustration that their participation is limited to commenting on text that has already been drafted in the industry panels (House Energy and Commerce Committee, 2003).

Limiting governmental flexibility in order to reduce barriers to trade

Traditionally, free trade treaties have been limited to national level rules directly related to trade; however, NAFTA is extended to *all* rules, regulations, or guidelines that may incidentally favor domestic production over foreign competitors (NAFTA, Article 201). This can include subnational rules regarding licensing, environmental standards, zoning, limiting the number of businesses through needs tests, demanding performance requirements or employee training to ensure benefit to the community from new businesses (Bottari and Wallach, 2001). All modern trade agreements attempt to make laws more uniform (*harmonization*), to reduce uncertainty and lower transaction costs for foreign investors. This process of harmonization results in either all countries having one set of regulations or each party accepting each other's different laws as comparable (Wallach and Sforza, 1999).

In the US federalist system, there has historically been deference for state law and an acceptance that local governments are more representative of local preference (Lowi and Ginsberg, 2000). The federal Environmental Protection Agency, for example, sets the floor for environmental standards to protect human health, and the states may have more stringent standards (Rausser, 2002). Harmonization undermines this diversity.

Redefining private property

Traditionally, investment chapters were included in treaties to restrict party countries from nationalizing private property. The NAFTA investment chapter 11 goes a step farther by empowering foreign investors to bring nations into international arbitration to defend government measures that affect their private investments (property) negatively, and redefining property to include future profits, market access and market share (Mann and von Moltke, 1999; Bottari and Wallach, 2001). An 'investor' is any person, company or lender with a financial stake in a venture that sells goods or services in a participating country where the investor is considered foreign (NAFTA, Article 1101). These are both significant shifts in traditional powers. In the US, states have traditionally defined property and the rules regarding the balance between private rights to use property and the public good. NAFTA defines the property rights for foreign investors and shifts the responsibility for enforcing host nation obligations to commercial investors.

As well as redefining property to include any investment such as a loan to a company or shares in a corporation (NAFTA, Article 1138), a key feature of the new trade agreements is the change in definition of what constitutes a government 'taking' of property. Typically, governments are allowed to limit the use of private property for public use when the public need overrides private interest. Property in the US, for example, is often affected by environmental regulations and zoning, and some restriction on use is a reasonable loss in exchange for the privilege of citizenship (Dalton, 1999). In the US context, loss of use of the property in its *entirety* gets compensation, but partial losses in property value (even as great as 95%) are insufficient to be compensable (Lowi and Ginsberg, 2000; Eagle, 2001). If there is an economically viable use of the property other than the one preferred by the owner, it is

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not a taking (Thompson, 1995). Under NAFTA, partial losses of profit or use of property due to government taking (in physical form or via regulations) may require government compensation (Appleton, 1994; Kuehl, 2001a).

Adjudication process

Investor access to international tribunals is another shift that raises private foreign investors to a peer level with nations. This status can be used to challenge or influence traditional governance measures (Greider, 2001a), including legislation, the domestic court decisions, and the acceptable balance of private and public interests (Kuehl and Machado, 2001). NAFTA gives US investors the authority to engage Mexico and Canada in legal battles over private property rights and profit, and their investors to challenge US government measures.

NAFTA drafters sought to identify an adjudication process that would be efficient, respect the different interests of affected parties and the proprietary nature of commercial information. Rather than subject foreign investors to the differing standards of domestic courts or the potential for corruption or political interference, the NAFTA adopted an arbitration approach used in commercial agreements. In effect, this system replaces domestic processes with international courts and law, shifting disputes regarding domestic state matters to an international venue.

Each party nation to the NAFTA agreement waives immunity for all levels of government and the right to hear complaints within the national court system (De Palma, 2001). There are three members in the tribunal — a representative chosen by the nation, one by the investor and a third arbitrator jointly selected (Mann and von Moltke, 1999). The parties then choose the standard of law that will be used to decide the controversy, but both NAFTA and the General Agreement on Trade in Services (GATS) specifically suggest international standards be followed (GATS Article VI.5b). In keeping with commercial protocols, the arbitrations are held in secret (to protect investors) and results are only made public if both parties agree. The arbitration rules have not been altered to recognize the public character of disputes.

This adjudication process represents a significant departure from historical US government practice. The 11th amendment of the US Constitution reserves to the state the right to defend the state from foreign claims. One foundation of the US court system is a requirement to give court law of the local jurisdiction deference or access to the process, but the arbitration panels are under no requirement to do this (Eagle, 1997). A California Senate committee, formed specifically to investigate the impacts of trade agreements, has raised concerns that the investor right to settle disputes in an international arbitration process will have a negative impact on democratically formulated public and environmental health legislation (Kuehl, 2001b).

Implications of these governance features for subnational governmental authority

To better understand how these new governance provisions in NAFTA affect subnational government action, we look at two cases: Methanex in the State of California and Metalclad in Gualdalcazar, Mexico. These cases show how state and local governments can still employ traditional government powers (land use controls, legislation and judicial proceedings) but these may be trumped when a foreign investor appeals to a NAFTA tribunal. Both cases illustrate the narrowing of criteria in reviewing the legitimacy of government action — to the concerns of 'least trade restrictive' over concerns for public health or local democratic preference. It is not clear whether the national or subnational units will bear the financial costs of NAFTA decisions. However the costs to subnational democratic expression are clear. The NAFTA governance features rescale power to the executive over the legislative and judicial branches and to the federal over the subnational.

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Case study 2: loss of subnational power — California Methanex case

In 1997, a California State Senate study, requested in response to citizen complaints, reported that methyl tributyl ethanol (MTBE), a chemical added to gas to make it more efficient, had contaminated at least 10,000 groundwater wells (Bottari and Wallach, 2001; Roosevelt, 2002). As MTBE is carcinogenic in lab animals and causes headaches and nausea in humans, the state weighed its options to avoid further contamination of public drinking supplies (US Statement of Defense). The study estimated the remediation costs of the existing damage to be $160 to $300 million (Roosevelt, 2002). Residents with tainted wells also had lost property value, found it hard to sell their homes, and had to buy bottled water (Moyers, 2002). Other gas additives are available that are less water soluble, and therefore less of a threat to water resources than MTBE (Rausser, 2002).

The state government sought to protect its citizens by avoiding future harm to water resources and property values, and some cities sued to clean the damage that was done and were rewarded by the courts. On 25 March 1999, California passed a resolution to phase-out MTBE by 2003 (Mehta, 2002). During this time, California cities sued refiners for ground water well pollution by MTBE and were awarded close to $40 million for remediation by US courts (Gullo, 2002; Kay, 2002; Mehta, 2002).

Methanex, a Canadian firm, is currently challenging the United States over the California ban in a NAFTA arbitration and is claiming US $970 million in damages including good will, reputation and future profits (Methanex Corporation Statement of Claim, 1999). Methanex's product, methane, is one of the components of MTBE. Under NAFTA, governments must regulate through the least trade restrictive means, and Methanex claims that the ban goes too far and expropriates their property — i.e. market access measured by potential future profits. Under NAFTA, Methanex has argued the state should have tightened up environmental inspections of underground tanks rather than eliminating the chemical (Lazar, 2000). The claim asserts that NAFTA limits government action to the choice that impacts the flow of goods and services the least, replacing the standard balancing test of public and private interests. Methanex also claims that the alternative additive, ethanol, is made by US manufacturers and therefore the ban prefers US companies at the expense of Canadian investors, violating NAFTA's national treatment obligation.

These claims would not be successful within the US legal system. First, the damage claim would not survive. Methanex is asking for a partial takings ruling based on the loss of 6% of their production. In the US system, property must lose nearly all of its value to require compensation for damages due to regulations. Second, most legislation bears the burden of being rationally related to a legitimate government objective. The US courts give great deference to the states' legislative intent, and allow states to have laws more stringent than the federal system. The NAFTA arbitration tribunals apply strict scrutiny that requires regulations affecting trade be narrowly tailored. Thus, the trade analysis has a singular focus on supporting free trade rather than considering common criteria (e.g. public health) used by subnational governments to balance competing objectives. Finally, in the US system the focus would be on the harm caused by the product, not the incidental positive impact on substitutes.

Methanex raises questions about the police power of the state to protect the residents and the potential for a 'chilling effect' on protective legislation. Warren Christopher, former US Secretary of State, has been assigned to defend US interests, which underscores the significance of the challenge. If the NAFTA claim were successful, the US would have to pay the polluter for their loss of business, or allow the chemical to be used and pay for better containment procedures to prevent pollution. In either case, the financial burden is placed on the government, not the manufacturer, and the threat of challenges may chill government action or innovation in regulatory structures. The federal preference for free trade is substituted for democratic legislative and judicial action at the subnational (state and local) levels.

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Case study 3: municipal level authority trumped — Mexico vs Metalclad

Brenner (2000) suggests that cities are increasingly forced to interact with international bodies without the buffer of the nation. However, close analysis of the NAFTA reveals that, though cities incur obligations under the agreement, they have no meaningful representation at the negotiating or dispute resolution tables (Mann and von Moltke, 1999). Nation-states are firmly in control of the formulation of the agreement, the implementation and the dispute resolution process — a process that the Metalclad case shows lacks transparency, citizen participation and open debate.

The Municipality of Guadalcazar, Mexico, was approached by a Mexican company named COTERIN that wanted to open a toxic waste facility. The land had already been polluted by toxic waste and the ground water was compromised (Shrybman, 2002). The federal and state governments either granted or promised the appropriate permits, and Metalclad, an American company, bought COTERIN on the understanding that it would obtain the necessary permits before the sale was final so that Metalclad could build the facility (Kass and McCarroll, 2000). The federal and state governments assured Metalclad that no further permits were required, but suggested for political reasons they contact the local officials. The state ecologist and governor of the Mexican State of San Luis Potosi expressed reservations about the tenfold expansion to the existing site and sent word that building should cease based on an environmental impact assessment that found the groundwater would be polluted by the operation (Mann and Arraya, 2002).

In 1994 the application for a local building permit was denied and state and local officials consistently held through 1995 that the facility should not be built. When the building was finished, Metalclad shareholders visited the facility and were greeted by protesters. In September 1996 the governor requested and was granted an injunction to the facility opening from the federal government (Kass and McCarroll, 2000). Before leaving office, the governor zoned the entire area a wildlife preserve in the hope that his successor wouldn't reverse his decision. After using the permit system, the court system, community activism and zoning, the facility was permanently closed.

In October 1996, Metalclad used the investor protection chapter in NAFTA to take the issue to international arbitration, claiming the change in zoning was an expropriation of their investment. As required by NAFTA rules, the American company brought the case, and the federal government defended San Luis Potosi's and Guadalcazar's interests. In the tribunal decision, neither the environmental damage nor the health risks of contaminated groundwater were discussed. The Tribunal referred to three NAFTA objectives to explain their interpretation of Chapter 11:

- Transparency in government regulations;
- Increased investment opportunities; and
- A predictable commercial framework for investors (IISD, 2001).

Only government action is restrained by international trade agreements, so the only action discussed was the final decision — the change in zoning. Though there were other uses for the property, the court decided that the investment was expropriated by the government and awarded Metalclad US $16.7 million (Metalclad Corporation v. United Mexican States, 2000). Judge Tysoe (2001) of British Columbia, one of the judges who reviewed the decision, voiced concern that this broad interpretation of the trade agreement could interfere with customary and legitimate zoning laws.

In the Mexican courts such an award would be unlikely as private property rights are subservient to the public good. Nor would Metalclad have been successful in a US court because the investment had alternative uses and partial takings are not compensable. The Mexican federal government is now trying to recoup the costs from San Luis

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Potosi.[2] The Metalclad case illustrates the differences in interests of national and local levels of government and how local government authority can be thwarted when it is not granted access to the adjudication process. The case suggests the Mexican federal government did not respect the clearly delineated authority of the local government (regarding permitting and zoning), and gave priority to the economic importance of protecting foreign business investments for trade reasons over local preference and concerns for public health.

The impacts of rescaling

These three cases illustrate the nature of the rescaling process at the national, regional and local levels. At the national level NAFTA has introduced international disciplines to limit the flexibility of national legislative and judicial systems. These decisions, made at the federal level, weaken judicial and legislative power at all levels, thus reducing democratic expression and shifting the balance of power to the executive or supranational institutions. At the subnational (state) level we see how NAFTA's harmonization and least trade restrictive goals narrow the criteria for legitimate government action and undermine legislative diversity and collective expression. The Methanex case challenges the legitimacy of state court decisions and shows the potentially high costs of partial takings claims. At the local level, the Metalclad case shows how NAFTA can affect basic local government authority (land use laws, permitting and zoning). The lack of voice or representation for affected local parties in the adjudication process reflects a severe erosion in democratic representation.

Our analysis of the NAFTA text and its early implementation as reflected in the Methanex and Metalclad cases, has illustrated the importance of this rescaling process and its implications for subnational authority. Loss of democratic voice results from the lack of adequate governance mechanisms to reflect the full diversity of interests — private sector, citizen and societal wellbeing (Wallach and Sforza, 1999). However, the governance deficit extends beyond this loss of mechanisms for democratic expression (Cerny, 1999).

Domestic governance and the choice of law

At its most fundamental level, government is about the ability to reflect collective preference and protect the public interest through the exercise of law. In a federal system, states and localities are given considerable discretion in the nature of the laws. This leads to a diverse landscape of land use and environmental protections, and tax and regulatory structures. Limitation in the choice of regulation undermines the legislative diversity allowed in a federalist system. If there is another choice that would allow the same level of protection (in the interpretation of a tribunal), but impact trade less, then the more restrictive law is in violation of the agreement (Charnovitz, 1992; Esty, 1994). Legal experts believe that the required harmonization under NAFTA will preempt the state's role in setting the acceptable risk (Stumberg, 2001).

In an effort to avoid challenges to domestic law, the trade agreements require that government actors communicate their proposed actions and allow foreign investors who may be directly or incidentally affected to comment (NAFTA, Article 1411). This invites current and potential foreign investors to be active in the legislative process of host nations (NAFTA, Article 1802; Stein, 2001). Access of this magnitude is a step toward greater cooperation, but foreign corporate concerns may dilute citizen voice (Greider, 2001b; King, 2002).

2 The financial liability of US states or localities in the same situation is unclear. There is no indemnification clause in the implementing language that protects states from being forced to give up block grants or other federal funding to pay for losses from arbitration.

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The imbalance of obligations under trade disciplines

Foreign investors can challenge the laws of cities, but the city does not have a right to participate in the defense. It is up to the individual tribunal whether or not they will entertain evidence and argument from a city that is being challenged (Methanex Corporation Draft Amended Claim, 1999). This is in contrast to the transparency requirements for domestic legislation and court activity. There is no obligation for the national government to tell the state legislature or locality that there is a claim at all (Greider, 2001a). Under NAFTA, foreign investors are given the right to enforce the obligations created in the agreement but have no corresponding obligations (Dalton, 1999; IISD, 2001). Municipalities, by contrast, have significant substantive and process-based obligations under the agreements that may be costly both financially and in terms of sovereignty and democratic practice (Stumberg, 1998; Kuehl, 2001b).

Dual legal framework undermines government consistency and stability

The most obvious threat to the stability of the court system is that no civil dispute with a foreign investor will be considered settled until a tribunal has also considered it. Furthermore, arbitration panels are not required to follow the precedent set by previous panels; each time an issue arises, it may be decided differently. Compounding this uncertainty, two standards for disputes would arise; one for foreigners set by NAFTA, and the traditional law for domestic investors (Stokes, 2001).

Ironically, the free trade agreements, while designed to promote neoliberal goals of privatization, are likely to make successful government contracting more difficult. When governments structure market contracts they need the security of a standard adjudication procedure should the contract fail. Open contracting requires the standards be similar for all contractors. Two different sets of laws (one for domestic contractors, and another — unpredictable one — for foreign firms) will make it difficult for governments to construct fair bidding processes or monitor and enforce contracts. Recall that trade agreements preclude governments from requiring foreign investors to satisfy performance requirements or other local benefits, creating a double standard between foreign and domestic contracting.

Similarly, the expansion in the definition of takings to include partial takings, or compensation for any loss of productivity due to environmental regulations or limitations on property use, is a significant expansion of government liability that values the private over the public. This is a greater right than US citizens have under the takings clause in the United States Constitution (Greider, 2001b), and is a novel concept to many nations that do not have such carefully defined private property rights. In Mexico, private property rights are subservient to the public need (Esty, 1994), thus a shift to a compensation scheme for the public use of land is not a matter of degree, but an entirely new cost for government. Some litigators suggest the partial takings liability would bankrupt many local governments or divert financial resources from critical public works (Kendall *et al*., 2000).

US takings legislation clearly shapes property owners' expectations of compensation for limits on private property use in favor of the public good (Trelease, 1971; Callies, 1996). In most instances, restrictions on property that affect all owners in the same fashion are not compensable (Eagle, 2001). If the agreements require foreign investors be paid for restrictions of general applicability, the costs may prohibit the action or develop a dual standard for domestic and foreign property owners (Stokes, 2001). Forced compensation for regulatory takings due to treaty obligations will undermine foreign investors' incentives to participate in voluntary market solutions — one of the key promises of privatization.

Making government pay private investors for the losses incurred as a result of government regulations will substantially undermine government action — especially in this era of market regulatory approaches where government more typically uses tools that create market incentives for private compliance rather than direct government

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provision (Salamon, 2002). Most state and local government regulations could be considered 'partial takings' under this expansive interpretation. Epstein (1985) first proposed this theory of regulatory takings, arguing that government actions such as zoning, environmental and labor regulations constitute takings. The basic land use controls employed by cities to control the number and types of businesses and buildings acceptable for an area could be challenged (Bottari and Wallach, 2001). Any preferences for local goods or labor are specifically prohibited by NAFTA, as are performance requirements to ensure benefit to the community. William Greider (2001b) argues: 'To enshrine this radical new definition of property rights would provoke a grave governing crisis, from local zoning laws to the (Supreme) Court's own legitimacy'.

Subnational government response

These new free trade agreements create a quandary for subnational governments. Given the pressures of the competitive state, subnational governments recognize the need to be entrepreneurial (Eisenger, 1988), and thus typically support free trade as a source of economic development (Jessop, 1997). The role US state and local governments play in facilitating economic development has distracted them from recognizing the important governance changes these agreements portend. For US cities the entrepreneurial concerns take precedence. By contrast, social cohesion plays a more dominant role in European cities (Le Galès, 1998; Fainstein, 2001) and national identity and culture are critical concerns for Canadian and Latin American cities.

The Canadian Union of Public Employees and the Council of Canadian Municipalities have been very critical of these agreements and have requested major revisions or repeal (CUPE, 2001). More recently, US state and local government associations (NCSL and NATT, 2001; NLC, 2002), have requested that the NAFTA Chapter 11 be revised and not used as a template for other agreements. The ability of state and local governments to eliminate the liabilities of the agreements is hindered by the lack of access to negotiating committees singularly focused on economic benefits. Despite the concerns expressed to the USTR and members of Congress, the FTAA draft currently under discussion contains a virtually verbatim replica of Chapter 11.

Throughout Latin America, the public is vocally protesting the lack of democratic access to the negotiations, corporate influence replacing public voice, and the perception that the agreements will create greater domestic inequities as foreign countries benefit (Butler, 2002, Forero, 2002). Though direct opposition to NAFTA was muted, civil society has been more vocal, protesting in the streets at each major round of FTAA talks. While urban scholars recognize the power of these new forms of engagement with global processes by local actors (Holston and Appadurai, 1999; Sassen, 2001), these forms of resistance also reflect the loss of other more formal and traditionally legitimate mechanisms for expressing collective interests, such as subnational legislation and the public courts system.

Conclusion

In this article we have shown how the new governance provisions of NAFTA are rescaling governmental authority, altering citizenship rights, and substituting private forms of negotiation and adjudication for public legislation and courts. These shifts are creating a new governance nexus comprised of global, national and private investor interests. The erosion of subnational voice and authority in these agreements challenges the potential for resurgence of the city under globalization. While the city may be involved in more direct negotiation with global corporations on some economic projects, its legal authority, at the same time, is being compromised by these new

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international governance protocols. This reality requires nuanced attention to the multiple scales in which governance structures are being constructed and dismantled in a dynamically changing global system. For example, while Guadalcazar had short-term success in its local resistance efforts, neither the city nor its citizens had any representation in the final adjudication process, yet they will pay the damages of the award. Similarly, California, in the Methanex case, is barred from the ongoing proceedings even though their laws and public health are at stake. This erosion in traditional subnational government power to represent and protect the public interest should be cause for concern.

These free trade agreements limit national regulatory authority by making national policy subject to international rules and protocols. However, the agreements also reassert national control over subnational expression in legislation and the courts system. The nation is required to take an active role to homogenize subnational rules to be consistent with international standards. Thus, while some argue the nation state is losing power both upward to the international level and downward to subnational units (Brenner, 1999), we see these international agreements actually strengthening national control over subnational governance. This complicates our understanding of the localization processes emergent under globalization. The unique differences that 'glocalization' portends (Swyngedouw, 1997) could be fundamentally undermined by the homogenization required under the free trade regimes.

The intersection of these multiple scales of governance is central to the urban question (Brenner, 2000). As our cases have illustrated, the contradictions between private profit and public interest are most directly experienced at the subnational level, however their resolution is primarily engaged at the global level between private investors and nation states. This loss of public voice at the subnational level and the enhancement of private authority at the global level should cause the governance deficit in these agreements to become more obvious. Some free trade proponents believe the agreements were drafted specifically to restrain the traditional role of subnational government (Appleton, 1994). However, David Price, Chief Negotiator for NAFTA, has argued any shifts in national and local governance authority are due to nations voluntarily giving up rights in order to achieve other goals permitted by freer trade (Greider, 2001b).

By vesting all the power of negotiation and dispute resolution only at the national, corporate and international scales, the ability of our governance structures to secure the public interest is undermined. 'Globalization is leading to a world in which cross-cutting and overlapping governance structures and processes increasingly take private, oligarchic forms; where hegemonic neoliberal norms of economic freedom and personal autonomy are delegitimizing . . . democratic governance' (Cerny, 1999: 2). The complexity of these new networked governance systems (which involve public and private actors at multiple scales) creates new challenges for representation, voice and accountability (Amin and Hauser, 1997; Salamon, 2002). Government retains the responsibility for assuring these features, but not the authority to secure them. Historically stable notions of western democracy — checks and balances between executive, legislative and judicial functions, democratic participation and transparency — are being swept aside. For some countries where private property has not been so heavily privileged, the interjection of these new governance concepts of private property and market independence represents a more radical departure from traditional notions of governance and the public good. These shifts in governance must become a more central focus for urban scholars.

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